United States Court of Appeals

for the Second Circuit

APPELLANT'S BRIEF

76-7616

United States Court of Appeals

For the Second Circuit

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P/S

In Re Franklin National Bank Securities Litigation

ROBERT GOLD, on behalf of himself and on behalf of all others similarly situated,

Plaintiff-Appellant,

and

LOUIS PERGAMENT,

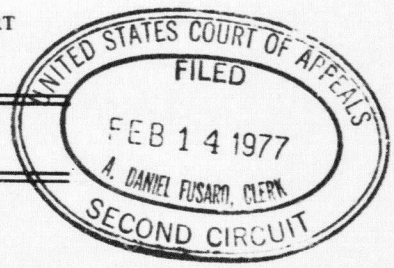
Intervenor-Plaintiff-Appellant,

against

ERNST & ERNST, HAROLD V. GLEASON, PAUL LUFTIG, PETER R. SHADDICK, MICHELE SINDONA, CARLO BORDONI, HOWARD D. CROSSE, ANDREW N. GAROFALO, DONALD H. EMRICH, and ROBERT C. PANEPINTO,

Defendants-Appellees.

ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE EASTERN DISTRICT OF NEW YORK



BRIEF FOR PLAINTIFFS-APPELLANTS

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UNITED STATES COURT OF APPEALS
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IN RE FRANKLIN NATIONAL BANK SECURITIES LITIGATION	:	
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-and-	:	
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Defendants-Appellees.	:	

PRELIMINARY STATEMENT

Plaintiffs-appellants ("plaintiffs") appeal from orders of the Honorable Thomas C. Platt of the United States District Court for the Eastern District dated October 27,

1976 and November 30, 1976 insofar as those orders required plaintiffs as class representatives to bear the costs and expenses of identifying beneficial owners of Franklin New York Corporation ("Franklin") securities registered in nominee name. Judge Platt's decisions have not been reported, and appear in the Joint Appendix at pages A222-A227 (Memorandum and Order dated October 27, 1976), A261-A280 (Order Certifying Class and Designating Manner and Time of Notice dated November 30, 1976), and pages A281-A283 (Supplemental Memorandum and Order dated November 30, 1976).

STATEMENT OF ISSUES PRESENTED FOR REVIEW

Did the District Court err in holding that a class representative's duty to provide individual notice of the action to class members who can be identified through reasonable effort imposes upon class representatives responsibility for effecting individual notice to unregistered owners of the subject securities and therefore requires class representatives to bear extremely burdensome expenses of identifying class members who, for their own or their nominees' economic benefit, have chosen not to register the subject securities in their own names?

STATEMENT OF THE CASE

(a) Nature of the Case and Course of Proceedings

Plaintiffs in Gold v. Ernst & Ernst, et al. (75-C-684) (hereinafter the "Gold action"),* have brought suit on behalf of purchasers of securities of Franklin -- the holding company which owned the Franklin National Bank -- to recover damages sustained by such purchasers in connection with the collapse of the Franklin National Bank. The amended complaint (A21-A44) alleges that the class sustained damages arising out of failures by defendants to disclose material facts concerning the results of operations and the economic condition of the Franklin National Bank in violation of Section 10(b) of the Securities Exchange Act of 1934, Rule 10b-5 promulgated thereunder, and the common law.

In a Memorandum and Findings dated April 5, 1976, Judge Judd determined that class certificiation in the Gold action was proper (Record on Appeal, Document No. 124 in

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* The Gold action was originally brought in the United States District Court for the Southern District of New York but was subsequently consolidated for pre-trial purposes with various other actions relating to the failure of the Franklin National Bank in the United States District Court for the Eastern District of New York under the caption In re Franklin National Bank Securities Litigation (M.D.L. #196).

papers filed under Gold, et al. v. Ernst & Ernst, et al.). Subsequent to Judge Judd's untimely death, the action was assigned to Judge Platt. On August 19, 1976 plaintiffs moved for an order certifying the action as a class action on behalf of all purchasers of common stock, preferred stock, or capital notes of Franklin who purchased any of such securities between July 16, 1973 and May 16, 1974, and also moved for determination of the form and manner of notice of pendency of class action (A45-A54). Plaintiffs' proposed order provided that notice would be mailed "by first class mail to members of the class or their nominees, at their last known addresses as they appear on the books and records of the Franklin", its transfer agent, or its trustee (A48). All forms of the order as proposed by defendants contained the same statement. (A65-A66; A104; A240) Plaintiffs' and defendants' proposed forms of notice were also in agreement in providing as follows:

> "Banks, brokerage firms, and other institutions holding record title as of any day from July 16, 1973 through and including May 16, 1974 to Franklin securities beneficially owned by others are required to forward this notice to the benefical owners." (E.g., A54; A250)

Despite defendants' agreement to an order which did not require plaintiffs to mail the notice to persons other than registered holders of Franklin securities, defendants proposed that the order certifying the class require plaintiffs to bear the costs of identifying class members who had not registered their securities in their own name but who had placed their securities in "street" or nominee name. Plaintiffs opposed such proposal on the grounds that (a) class representatives are not required to provide individual notice to persons other than registered owners; (b) the transaction in which stock is placed in street name constitutes a private arrangement between the nominee and his customer effected for their own purposes which should not result in a special burden for the class generally; (c) the nominees who foster and benefit economically from the system of nominee-name registration which conceals the identity of the beneficial owners should not be recompensed by class representatives for the special difficulties in identifying beneficial owners which the nominees themselves have created; (d) the nominees themselves have a fiduciary responsibility to transmit class notices to the beneficial owners; and (e) imposing such costs on class representatives

would severely impair the utility of class actions as a key device for protection of investors. (A82-A87; A179-A219)

In a Memorandum and Order dated October 27, 1976 (A222-A227), Judge Platt held that plaintiffs must bear the costs at issue. Judge Platt's opinion relied heavily on this Court's decision in Sanders v. Levy, ___F.2d___, 21 Fed. Rules Serv.2d 1213 (2d Cir., June 30, 1976) (slip opinion at A151-A171), petition for rehearing en banc granted September 14, 1976 and decision on rehearing presently sub judice, which Judge Platt interpreted as prohibiting the imposition of such costs on persons (such as nominees) who are not formally parties to the action. (A225-A226)

On November 5, 1976, plaintiffs moved for re-argument of the issue and requested that if the district court should reaffirm its decision it certify the issue for an immediate appeal pursuant to 28 U.S.C. §1292(b). (A228-A236) In a Supplemental Memorandum and Order dated and entered November 30, 1976, Judge Platt granted the motion to reargue and after further consideration adhered to his original decision (A281-A283). On the same date, Judge Platt signed and entered his Order Certifying Class and Designating Manner and Time of Notice (A261-A280), which in

paragraph 10 imposes upon the class representatives the costs of identifying beneficial owners of street or nominee name securities (A265).*

In his November 30, 1976 Supplemental Memorandum and Order, Judge Platt granted plaintiffs' request for certification of an interlocutory appeal

> "...on condition that (after the defendants furnish to the plaintiffs within 10 days after the date hereof a list of the known nominees) liason counsel at plaintiffs' expense (i) must furnish each of such nominees with a copy of this Court's Memorandum dated October 27, 1976, (ii) notify them that they are taking an immediate appeal to the Court of Appeals and (iii) advise them that they may wish to refer the matter to their counsel for appropriate action." (A282)

The Supplemental Memorandum and Order contains the following certification which it states, "will be deemed to be a part of the attached order [i.e., the Order Certifying Class and Designating Manner and Time of Notice] dated November 30, 1976":

> "The undersigned is of the opinion that the attached order involves a controlling question of law as to which there is substantial ground of

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* In the Order Certifying Class and Designating Manner and Time of Notice, Judge Platt certified the action as a class action on behalf of all persons who purchased Franklin securities during the period from July 16, 1973 to May 16, 1974 (A263).

> difference of opinion and that an immediate appeal from the attached order as authorized by 28 U.S.C. § 1292(b) may materially advance the ultimate termination of this litigation. It is ordered that all proceedings herein be stayed for 10 days from date of entry of this and the attached order. If, within such 10 days, the plaintiffs shall apply to the United States Court of Appeals for the Second Circuit for permission to appeal from this order and if the plaintiffs proceed as expeditiously as possible with such appeal, the proceedings herein shall be stayed pending determination of such application or of the appeal, if it is allowed." (A283)

On December 9, 1976, plaintiffs filed with this Court their Petition for Permission to Appeal pursuant to 28 U.S.C. §1292(b), and on February 2, 1977 this Court granted plaintiffs' Petition. In the interim, defendants provided plaintiffs with a list of companies which defendants stated might be nominees which purchased Franklin securities during the class period, and in compliance with Judge Platt's direction plaintiffs have mailed the required notice of their intention to take this appeal to each of the 661 companies on the list for which defendants were able to provide addresses. (A284-A290)

While plaintiffs sought permission to appeal under Section 1292(b) in order to forestall any possible question concerning the availability of an appeal as of right,

plaintiffs believe that the issue involved is appealable as of right under the "collateral order doctrine." E.g., Eisen v. Carlisle & Jacquelin ("Eisen IV"), 417 U.S. 156, 169-72 (1974); Sanders v. Levy, supra, 21 Fed. Rules Serv. 2nd at 1214, Slip Opinion, p.4580 (App. 154). Consequently, plaintiffs filed a Notice of Appeal on December 9, 1976 (A19) and proceeded promptly to docket and perfect the appeal prior to this Court's grant of permission to appeal.

(b) Facts Relevant to the Issue Presented For Review

1. Nature and Scope of the Nominee Name System of Securities Registration

The issue at bar arises because persons purchasing securities sometimes fail to register such securities in their own names and leave them in the name of a nominee such as a brokerage firm, investment company, insurance company, or bank. According to a recent SEC report

> "The practice of registering securities in the records of issuers in other than the name of the beneficial owner is commonly referred to as 'nominee' and 'street' name registration. Nominee name registration refers to arrangements used by institutional investors (insurance companies and investment companies among others) and financial intermediaries (brokers, banks and trust companies) for the registration of securities held by them for their own account or for the account of their customers who are the beneficial owners of the

> securities. Street name registration, a specialized type of nominee name registration, refers to the practice of a broker registering in its name, or in the name of its nominee, securities left with it by customers or held by it for its own account." SEC Street Name Study: Final Report to Congress, CCH Fed.Sec.L.Rep. No. 672, December 15, 1976, Part II ("Street Name Study II"), page 1 (footnote omitted)

Extensive use of nominee registration began to develop in the 1930's in an effort by nominees to escape from having to reveal their status as fiduciaries when effecting transfers of stock beneficially owned by others. Nominees sought to conceal their fiduciary relationship because of transfer requirements placed on fiduciaries by issuers aimed at protecting the issuers from judicially imposed liability for improper transfers. See Street Name Study II, supra, pages 1-2; SEC Street Name Study, Preliminary Report of December 4, 1975 ("Street Name Study I"), CCH Fed.Sec.L.Rep. No. 619, Part II, pages 6-7. By adopting the system of nominee registration, fiduciaries hoped to avoid the force of the so-called Lowry doctrine, which evolved from Lowry v. Commercial and Farmers' Bank, 15 F.Cas. 1040 (No. 8581) (C.C.Md. 1848) and was subsequently adopted by the Supreme Court in Duncan v. Jaudon, 82 U.S. (15 Wall.)

165, 175-76 (1872). Lowry required issuers to protect beneficial interests by verifying a fiduciary's authority to effect a particular transfer prior to the issuer's recognizing a transfer of ownership. According to the Securities and Exchange Commission ("SEC").

> "The use of the nominee as the registered holder of stock eliminated from the issuer's records any evidence of a fiduciary relationship and made the recordholder a non-corporate entity. Thus nominees could transfer securities without meeting the requirements placed on corporate or fiduciary shareholders." Street Name Study II, supra, pages 2-3 (footnote omitted).

Since the 1930's, the system of registering stock in nominee name has burgeoned, and as of 1970 the New York Stock Exchange data indicated that financial intermediaries other than brokers held in nominee name approximately 18.1%, and brokers held in nominee name approximately 8.6% of the common and preferred shares of canvassed public corporations. Street Name Study I, supra, page 8. As shown below, the increasing prevalence of nominee registration no longer constitutes simply an effort to escape the Lowry doctrine, but reflects immense economic benefits reaped by the securities industry from the system of registering securities in nominee name.

The United States Congress has recognized that the masking of beneficial ownership by nominee registration raises problems concerning effective implementation of the securities laws and facilitation of communications between issuers and beneficial owners. As a result, the Congress directed the SEC to study the nominee-name system in Section 12(m) of the Securities Exchange Act of 1934, and the SEC has recently completed a report in response to the Congressional direction. Street Name Study I, supra; Street Name Study II, supra. In its report, the SEC determined that the system of nominee registration is an integral part of the workings of the securities industry which benefits investors and the securities industry through facilitating the transfer of record ownership and the clearance and settlement of securities transactions. E.g., Special Study II, supra, pp. 3, 5. However, the SEC also recognized that "the widespread use of nominee registration . . . has collateral effects which may be disadvantageous," noting that the system renders "communications between issuers and their shareholders more circuitous due to the interpositioning of intermediaries" and that "it tends to complicate regulation by masking beneficial owners of securities." Street Name Study II, supra,

page 3. In consequence, the SEC has proposed that certain steps be taken to mitigate such problems and is engaged in a continuing study of the system in that regard. E.g., Street Name Study II, supra, pages 5-10, 63, 76, 80.

2. Nominees Reap Extensive Financial Benefits From Registering Securities in Nominee Name

The nominee name system enables nominees to substantially increase their profits. Use of street name permits brokers to minimize their expenses and overhead incident to the transfer and registration of securities:

> "Registration of certificates in nominee and street name facilitates the completion of securities transactions by institutions and brokers. It eliminates the need for numerous routine transfers by enabling brokers to deliver securities without the necessity of first transferring record ownership. Under industry practice, a buying broker will accept delivery from a selling broker of securities registered in street name (though not necessarily in the selling broker's street name), and a buying broker in turn may redeliver such securities to another broker, in each case without the need to transfer record ownership prior to delivery." Street Name Study I, supra, p. 15.

The use of nominee name permits brokers to engage in profitable sales of their customers' securities purchased on margin and held by the brokers as collateral for the margin loan:

> "A stockbroker who purchases stock for a customer dealing on margin has the implied right, in the absence of an agreement to the contrary, to sell the stock, provided he retains in his possession and control the equivalent in kind and amount which will be available to the customer in the event the customer desires to close the account and take away the securities to which he may be entitled. This right is implemented by placing the purchased stock in street name so that it can be effectively transferred by the broker". 6 N.Y. Jur. Brokers, §65 (1959) (emphasis added)

Placing securities in nominee name also facilitates short sale transactions in which a broker borrows and sells nominee name securities, remitting the proceeds to the lending broker as collateral for the loan, which lending broker earns valuable interest income on the collateral or makes other use of such funds until the shares are returned. See Cohen and Zinbarg, Investment Analysis and Portfolio Management (Richard D. Irwin, Inc. 1967), p. 67.

Substantial additional benefits accrue to brokers from nominee name registration because the issuers forward dividends directly to the broker as record owner. The broker then deposits such dividends in the customer's free credit balance and proceeds to make extensive and lucrative use of that balance:

> "As discussed below, apart from the requirements of a few states there are no regulatory restrictions on the use of free credit balances, and they are used freely by many firms to meet cash needs of the business. As might be expected, the use of these funds, on which generally no interest is paid, provides an important source of income for the broker-dealer. Broker-dealers employ free credit balances to maintain positions in securities, to carry on trading activities for the firm's own account or in connection with the firm's market-making functions and underwriting activities. Such funds also may be used to make loans to margin customers or to other broker-dealers." Hamer H. Budge [the then-Chairman, Securities and Exchange Commission], Broker-Dealer Financial Responsibility Requirements, 7 Idaho L. Rev. 151, 153 (1970). See generally, Id., 152-53, 165-168. (hereinafter cited as "Budge")

See also, SEC Report of Special Study of Securities Markets, Chapter III, Part D, pp. 15-22 (1963) (hereinafter cited as "Special Study").

As of the end of April 1970, New York Stock Exchange member firms alone held about $2.2 billion in free credit balances. Budge, supra, at 153. In its annual report to the SEC for 1961 Merrill Lynch, Pierce, Fenner and Smith, Inc. represented that it alone held approximately $233 million in free credit balances. Special Study, supra, Chapter II, Part D, p.17. Income and expense reports filed by New York Stock Exchange members doing public commission business in 1960 showed that 13% of their gross income was

derived from interest received from customers' balances. Ratner, Regulation of the Compensation of Securities Dealers, 55 Cornell L.Rev. 348, 387 (1970).

3. Requiring Class Representatives To Pay the Large Sums Claimed By Nominees To Be Their Expenses of Identifying Beneficial Owners of Nominee Name Securities Would Create a Major Impediment to the Prosecution of Securities Class Actions

Melvyn I. Weiss, Esq. -- an attorney who has been actively engaged in securities class action litigation throughout the United States for years -- apprised the District Court below of his firm's experience with respect to efforts by nominees to obtain reimbursement for the costs at issue. (A82-A86; A203-A206) Until recently, nominees did not question their obligation to forward notices to class members without reimbursement from class representatives, but within the past year the brokerage community has commenced a practice of sending bills to class representatives for reimbursement of such costs. (A83-A84; A204-A205) Mr. Weiss' affidavit attached as a typical example a letter from a brokerage firm seeking $500.00 for two hours of computer time required for searching the broker's computer for the names of beneficial owners in connection with

transmission of class notices in In Re Consolidated Pretrial Proceedings in Ampex Securities Case, Master File No. C-72-360 S.W. (N.D.Cal.)* (A207-A208). Mr. Weiss further stated:

> "It is quite possible that once having performed the search, E.F. Hutton will come up with but a few names of beneficial owners during that period. Prior to conducting the search, there is no way of determining how many members of the class are involved.
>
> "6. It is not difficult to conclude that an order directing reimbursement for the costs of computer searches and mailings to beneficial owners of all nominees listed in transfer records may well amount to an enormous sum of money even in a case where a relatively small number of class members exist. Regardless of whether a broker will ultimately identify two such customers or 500 such customers during a relevant period, the cost to make the computer search will be the same.
>
> "7. Our experience indicates that the typical stockholders list will include anywhere from 50 to 200 names of nominees. An average cost of $200 per nominee will run anywhere from $10,000 to $40,000. I have even received bills from some brokers at the rate of $300 per year of search in situations where the class period ran close to three years, thereby creating a possible burden in excess of $200,000 for such searches." (A204-A205) (Emphasis added)

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* As described at pages 31-32 below, the Court in the Ampex litigation has since rejected such broker's request for reimbursement in a ruling from the bench, a transcript of which ruling is annexed to this brief as Exhibit B.

In the present lawsuit Mr. Weiss' estimate of the number of nominees involved may well be too low, since defendants have subsequently provided plaintiff with a list of 661 companies which defendants believe may have been nominees during the class period. (A284-A288) Consequently, requests for reimbursement could well exceed $120,000 in the present action if the average cost per nominee is $200.

The imposition of such an enormous financial burden on class representatives would severely restrict the utility of class actions as a device for protecting investors. Plaintiffs submit that the applicable precedent does not require such a crippling impediment to class actions and that the costs involved are properly borne by the nominees who have created and benefit so substantially from the system of nominee name ownership or their customers who choose to place their stock in the name of another.

ARGUMENT

PERSUASIVE PRECEDENT AND SOUND PRINCIPLES OF PUBLIC POLICY COMPEL THE CONCLUSION THAT THE RESPONSIBILITY OF CLASS REPRESENTATIVES WITH RESPECT TO PROVIDING NOTICE TO THE CLASS DOES NOT INCLUDE REIMBURSING NOMINEES FOR THEIR EXPENSES IN IDENTIFYING CLASS MEMBERS WHO HAVE CHOSEN TO PLACE THEIR STOCK IN NOMINEE NAMES

In Eisen IV, supra, the Supreme Court held that in class actions brought under Rule 23(b)(3) the class

representative need only bear initially the cost of providing "individual notice . . . to all class members who can be identified with reasonable effort." 417 U.S. at 177 (footnote omitted) (emphasis added). That ruling was predicated upon an interpretation of the federal constitution and of Rule 23 concerning the requirements of notice in class actions. Plaintiffs submit that under the analysis of the Supreme Court in Eisen IV and the authorities upon which Eisen IV relied, neither constitutional "due process" considerations nor Rule 23 requires class representatives to mail individual notices to owners of Franklin securities not listed on the books and records of Franklin or its transfer agents. Consequently, plaintiffs' status as class representatives does not require plaintiffs to bear the costs at issue. As shown below, the weight of authority correctly holds that the costs at issue should properly be absorbed by those persons who in various private transactions utilize and benefit from the system of nominee name registration -- i.e., the nominee and/or his customer -- and not by the class representatives whose efforts to communicate with the

class are impeded by the system the nominees have created for their own benefit.*

POINT I

PLAINTIFFS FULFILL THEIR DUTY WITH RESPECT TO PROVISION OF INDIVIDUAL NOTICE TO CLASS MEMBERS BY MAILING THE NOTICE TO REGISTERED OWNERS OF FRANKLIN SECURITIES

(a) The "Due Process" Clause of the Federal Constitution Does Not Require That Plaintiffs Mail Individual Notice To Unregistered Owners of Franklin Securities

The Supreme Court in Eisen IV emphasized that its holding that "Individual notice must be sent to all class members whose names and addresses may be ascertained through reasonable effort" was compelled by constitutional due process requirements to which class action procedures were subject and which Rule 23(c) was designed to reflect. 417 U.S. at 173. See Advisory Committee's Note to Rule 23, 39 F.R.D. 69, 107 (1966). Eisen IV did not, however, interpret the Constitution to require class representatives to mail

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* While plaintiffs believe that they are not legally responsible for any of the costs of retransmitting the notice to unregistered beneficial owners, plaintiffs took the position below that they would not resist reimbursement of nominees for mailing costs and would provide extra copies of class notices to nominees at plaintiffs' expense, and have challenged in this action only the imposition of identification costs.

individual notice to all class members, but only to those who could be identified "with reasonable effort" and in consequence individual notice was required in Eisen IV only for slightly over one-third of the class. See 417 U.S. at 166-67.

Both Eisen IV and the Advisory Committee's Note on Rule 23 rely heavily for their interpretation of constitutional and statutory notice requirements on Mullane v. Central Hanover Bank & Trust Co., 339 U.S. 306 (1950), a case which strongly supports the conclusion that plaintiffs herein are not required to seek out and identify unregistered owners. While in Mullane the Court held that publication notice did not satisfy due process requirements where names of the beneficiaries of a common trust fund which was settling its accounts were known, Mullane also held that individual notice was not required as to beneficiaries who, "although they could be discovered upon investigation, do not in due course of business come to [the] knowledge of the common trustee." 339 U.S. at 317. See also, In re Randolph-Wells Building Corp., 332 F.2d 963 (7th Cir. 1964), cert. denied sub nom Boese v. Randolph-Wells Building Corp., 379 U.S. 963 (1965) in which the Seventh Circuit, relying upon

the above-cited language in Mullane, held that a notice to bond holders concerning the date for exchanging existing bonds for new bonds in a reorganized corporation complied with due process requirements when the notice involved was mailed only to registered owners of the bonds. 332 F.2d at 966-67.

Just as due process considerations did not require the trustees in Mullane and In re Randolph-Wells Building Corp. to mail individual notice to persons whose beneficial interests were not reflected upon the books and records of the subject corporation, the class representatives herein are not required to provide notice to beneficial owners of securities who have chosen not to record their ownership of such securities with the issuer.

Such a conclusion is reinforced by the special safeguards which protect the interests of unregistered beneficial owners in securities class actions even if notice is not mailed to them by the class representatives. Aside from the continuing power of the court under Rule 23(c)(1) to review the adequacy of the representation provided to the class, it should be recognized that the registered owners of securities include many sophisticated investors (such as

banks, investment advisors, brokers, and insurance companies) which will take a close interest in the class action so as to protect their own interests as beneficial owners as well as the interests of their customers. Moreover, as shown below, nominees have a fiduciary responsibility to assure that the beneficial owner does not remain in ignorance of important class notices. Indeed, the Supreme Court in Mullane v. Central Hanover Bank and Trust Co., supra, stressed that under such circumstances individual notice to all beneficiaries was not constitutionally required:

> "This type of trust presupposes a large number of small interests. The individual interest does not stand alone but is identical with that of a class. The rights of each in the integrity of the fund and the fidelity of the trustee are shared by many other beneficiaries. Therefore notice reasonably certain to reach most of those interested in objecting is likely to safeguard the interests of all, since any objections sustained would inure to the benefit of all. We think that under such circumstances reasonable risks that notice might not actually reach every beneficiary are justifiable." 339 U.S. at 319 (emphasis added)

(b) Individual Notice by Class Representatives to Registered Owners of Securities is Sufficient Individual Notice Under Rule 23

Rule 23(c)(2) provides, inter alia, that in class actions maintained under Rule 23(b)(3),

> "[T]he court shall direct to the members of the class the best notice practicable under the circumstances, including individual notice to all members who can be identified through reasonable effort."

As noted above, the Supreme Court in Eisen IV gave meaning to Rule 23's reference to what was "practicable under the circumstances" and to its limitation of the individual notice requirement to "members who can be identified through reasonable effort", and consequently the Court only directed that individual notice be mailed to slightly more than one-third of the total class. 417 U.S. at 166-67.

While under Eisen IV class representatives must initially bear the cost of notice to the class, plaintiffs would not have to bear the expenses of identifying beneficial owners of nominee name securities if the identification of such beneficial owners for the purpose of sending them the class notice is not "practicable under the circumstances" and would necessitate more than a "reasonable effort" by plaintiffs.*

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* Under this Court's decision in Sanders v. Levy, supra, expenses of identifying record owners of securities are considered a part of the expense of notice rather than an expense akin to other discovery expenses (with respect to the allocation of which the district court has discretion). Pending any revision of the Sanders v. Levy, supra, decision as a result of the current reconsideration en banc, the existing Sanders v. Levy decision is, of course, the law in this circuit. Plaintiffs do note that reversal or modification of the Sanders v. Levy opinion by this Court en banc would fundamentally change the issue in the present action if this Court en banc determined that the costs of identifying registered owners are not part of the cost of notice.

In the present instance, plaintiffs and defendants agreed that notice shall be mailed to the class members as they appear on Franklin's books and records, and the order certifying the class in no way states that plaintiffs are required to mail the notice to beneficial owners. Consistent with a nominee's fidicuiary responsibility to the beneficial owner of a nominee-name security (see discussion below, pages 40-43), plaintiff proposed and defendants agreed that the notice of pendency of class action instruct nominees to retransmit the notice to beneficial owners (A54; A250), and plaintiffs will provide additional copies of the class notice to nominees upon request. Such form of notice both recognizes that the class representative's responsibilities are limited to mailing the notice to registered owners and alerts the nominee to its own responsibilities.

The District of Columbia Circuit and the Tenth Circuit have held that the mailing of class notices to record holders of securities only, with instructions in the class notice to nominees informing them of their responsibilities with respect to beneficial owners, is consistent with notice requirements as enunciated in Eisen IV. In re National Student Marketing Litigation v. The Barnes Plaintiffs,

530 F.2d 1012 (D.C.Cir. 1976); In re Four Seasons Securities Laws Litigation, 63 F.R.D. 422 (W.D.Okla. 1974), aff'd, 525 F.2d 500 (10th Cir. 1975). In In Re National Student Marketing Litigation, individual notice was mailed to all shareholders of record during the class period, and 3,777 additional notices were requested by brokerage firms and other institutions listed as shareholders of record for forwarding to beneficial owners. The Barnes plaintiffs, including thirty-one street name purchasers, sought relief from court-approved settlements, arguing that the notice was defective since plaintiffs had not mailed copies of the class notice to them. The District Court rejected this contention, finding that "reasonable and diligent efforts were pursued to extend the class notice to brokerage firms where shares of stock were held in street name." 530 F.2d at 1015 (footnote omitted). The District of Columbia Circuit expressly affirmed this finding (Ibid.) and stated that "reasonable and orderly procedures were employed to identify and notify those NSMC stockholders composing the Garber and Natale classes." 530 F.2d at 1014.

In In re Four Seasons Securities Laws Litigation, supra, a street name purchaser moved for relief from a

court-approved settlement on the ground that he had not received adequate notice to allow him to "opt-out" of the action or object to the proposed settlement. Under the notification procedure adopted by the District Court, brokerage firms listed as record owners of the subject securities were given the option of either (a) revealing to the Trustee in Bankruptcy of the Four Seasons companies the identities of their street name customers for notification directly by the Trustee, or (b) forwarding copies of the notice provided by plaintiffs directly to their customers. The District Court concluded that this procedure constituted

> "the best notice practicable under the circumstances, that adequate provision had been made for individual notice to all members of the classes who could be identified through reasonable effort, and that such notice met all the requirements of Rule 23. The court adheres to that finding and conclusion." 63 F.R.D. at 427 (emphasis added)

The District Court also expressly held that the notice procedure employed was consistent with the requirements of Eisen IV. 63 F.R.D. at 430. The Tenth Circuit affirmed, holding that the notice afforded the street name purchaser was "far more than adequate" and "well within bounds as a discretionary matter for the trial court." 525 F.2d at 503.

In In re Clinton Oil Company Securities Litigation, M.D.L. #137 (D.Kan., January 8, 1975), Chief Judge Brown ruled (opinion unreported):*

> ". . .[W]e are of the opinion that under Rule 23(c)(2) and Eisen v. Carlisle and Jacquelin, ___U.S.___, 42 U.S.L.W. 4804 (1974), those members of the classes 'who can be identified through reasonable effort' and, thus, who should receive actual notice, are those members whose securities were registered on the books of Clinton Oil Company during the relevant times alleged in the complaints. A portion of the securities involved, we are informed, were registered in 'street name,' that is in the name of a broker/dealer for the benefit of the owner. Although it may be possible to trace the ownership of the stock through the ledgers of the various broker/dealers and thereby give notice to the beneficial owner, such an effort would be unreasonable and not practicable. We are satisfied that the 'process,' as stated in Eisen, that is due to the beneficial owners of securities held in 'street name' is actual notice to the registered owner and constructive notice to the beneficial owners by publication." Opinion at p.30. (emphasis added)

Plaintiffs submit that the above decisions are correct and that requiring class representatives to provide individual notice to unregistered owners of securities would

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* Copies of pages 1 and 30 of the opinion in In re Clinton Oil Company Securities Litigation are annexed as Exhibit A to this brief. Plaintiffs are informed that an appeal from such decision was dismissed by the Tenth Circuit as premature in an unreported opinion, and that a motion for reconsideration of such dismissal is pending.

go beyond the "reasonable effort" standard of Rule 23.* Numerous factors which support such a conclusion are discussed in detail in Point II(c) below, including (a) the widespread recognition under state law that notice to record owners is sufficient notice as to beneficial owners and that the record owner is, in fact, the owner of the securities involved for purposes of asserting important corporate rights; (b) the nominees' fiduciary obligations to retransmit the notices; (c) the unfairness of the nominees' shifting to class representatives the special burden of identifying beneficial owners which the nominees created for their own purposes and benefit in private agreements with beneficial owners to which the class members generally were not parties.

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* In Jahre v. Rait, No. 74 Civ. 805 (E.D.N.Y.), a group of nominees sought to challenge an order of Judge Weinstein requiring nominees to transmit a class notice without provision for reimbursement. The question became moot by virtue of a Court order filed October 30, 1976 on consent of the parties which found that prior efforts to notify class members were adequate without further forwarding.

POINT II

CLASS REPRESENTATIVES ARE NOT REQUIRED TO BEAR THE COSTS OF IDENTIFYING BENEFICIAL OWNERS OF NOMINEE NAME SECURITIES

(a) The Weight of Authority Holds that Such Costs Are Not Properly Imposed on Class Representatives

With the exception of the decision below and one other decision,* both of which (as shown below) proceed upon a misinterpretation of this Court's decision in Sanders v. Levy, supra, the Courts which have dealt with the issue at bar, to plaintiffs' knowledge, have held that class representatives are not required to pay the costs of identifying the beneficial owners of nominee name securities.

In In Re Penn Central Securities Litigation, M.D.L. #56 (E.D.Pa., June 21, 1976), appeal pending (opinion unreported; the relevant pages of the opinion appear at A200-A202), Chief Judge Lord denied the requests of various brokerage firms to be reimbursed for their expenses incurred in forwarding copies of a class notice to their customers. The Court recognized the inequity of requiring the entire

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* Weiss v. Drew National Corp., 75 Civ. 4816 (July 15, 1976) (opinion unreported; a copy of the opinion appears at A172-A175), motion for reconsideration granted and original opinion affirmed, November 18, 1976.

class, which includes those who chose not to purchase in street name, to bear extra costs made necessary because of an agreement between some class members and their brokers to utilize street name registration:

> "Nothing the brokers have pointed to in their brief convinces us that the class fund should bear the costs of forwarding the documents involved. Neither trade custom nor the inapposite holding of the Supreme Court in Eisen IV, supra at 179 overcomes the very obvious and common sense logic that if the brokers are to be reimbursed, it should come -- if at all[38] -- from the individual beneficial owners involved -- not the entire class. There is simply no reason to require the entire class to pay for the choice of a few to have their stock held in street name." (emphasis added)*

In a recent ruling from the bench, Judge Spencer Williams of the Northern District of California denied an application by a brokerage firm for reimbursement of the costs of identifying beneficial owners of street name securities in connection with the dissemination of a class notice. Judge Williams stated:

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* The Court's footnote 38 reads as follows:

> "We are not faced with, and do not decide, the obligation of the beneficial owner vis a vis the brokerage houses which held the stock in street name."

> "Well, it is a very interesting question, but I would say that the last group to have paid the cost of extra efforts to search out those who own the stock that are held in street name would be the class. The primary person responsible should be the shareholder who is going to benefit by the judgment. And if E.F. Hutton and Company cannot by virtue of its authority or its power, either one, get reimbursement from their clients or former clients, I think then the burden is with them. The motion [for reimbursement] is denied." Transcript of November 15, 1976 Hearing in Kushner v. Ampex Corporation, C 72-360 SW, p.16.*

The precise issue before this Court also arose in In re Clinton Oil Company Securities Litigation, M.D.L. #137 (D.Kan. 1976) and Chief Judge Brown ruled that broker-dealers holding securities in the subject company in street name were not entitled to reimbursement for their expenses of identifying and retransmitting class notices to the undisclosed beneficial owners:

> "After review of the Report and Motion filed by the Representatives (Dkt. 908), the Court determines that it is the initial duty of the Representatives to mail Notice and Proof of Claim form to the broker who is the record owner and holds legal title to securities, and that it is the duty of the broker to give notice to the beneficial owners. See Eisen v. Carlisle & Jacquelin, 417 U.S. 156, 40 L.Ed.2d 732 (1974); Greenfield v. Villager Industries, Inc., 483 F.2d 824 (3d Cir. 1973).

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* A copy of page 16 of the transcript of the November 15, 1976 Hearing is annexed to this brief as Exhibit B.

"When the Broker submits a list of names and addresses to the Representatives, disclosing the identity of the beneficial owners of the securities, it then becomes the duty of the Representatives to forward the Notice and Proof of Claim form to each such beneficial owner.

"In the event a broker requests additional supplies of notices and proofs of claim forms for forwarding to the beneficial owners of street-name securities, the Representatives may then provide such forms to the broker. Mullane v. Central Hanover Bank & Trust Co., 339 U.S. 306, 94 L.Ed. 865 (1950). However, the cost or expense incurred by a broker in preparing a list of names, or in forwarding the Notices on behalf of his beneficial owners, is a cost or expense to be borne by the broker in conducting his business, and not by the members of the plaintiff classes. See Blank v. Talley-Industries, Inc. (S.D.N.Y. 1972) 54 F.R.D. 627." Order and Instructions Concerning Notice to Brokers, April 5, 1976, pages 1-2 (Unreported)*

Prior to Eisen IV, the issue presented herein was considered by then District Judge Gurfein in Blank v. Talley Industries, Inc., 54 F.R.D. 627 (S.D.N.Y. 1972). Judge Gurfein ruled that Merrill Lynch, Pierce, Fenner & Smith was not entitled to reimbursement of expenses to be incurred in complying with a subpoena duces tecum in a class action requesting names and address of certain stockholders of General Time Corporation as shown on Merrill Lynch's records. Judge Gurfein stated:

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* A copy of Judge Brown's Order and Instructions Concerning Notice to Brokers is annexed to this brief as Exhibit C.

> "In view of the number of brokerage firms involved in the plaintiffs' court-ordered quest for class members' identities, it would be unfair to compel the plaintiffs to cover the costs of the firms' production of information, which costs when cumulated would indeed be burdensome. No other broker has requested reimbursement. In this class action I do not feel compelled in my discretion to require plaintiffs to pay the expenses of Merrill Lynch. These expenses are in the nature of overhead expenses necessary for responding to legitimate court orders involving the customers of stock brokers. Cf. Control Data Corp. v. International Business Machines Corp., 68 Civ. 312 (D. Minn. 1971) (pre-trial order no. 9, paragraph 5). Merrill Lynch should provide the required information on or before April 26, 1972." Id. at 627.

The ruling in Talley thus recognizes that brokerage firms properly absorb such expenses because they benefit from the system of operation which gives them control of such information. Moreover, the Court expressly stated its concern over the prospective cumulative financial impact of the requested ruling on the class representative.* While

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* The relative financial abilities of plaintiff and Merrill Lynch to absorb the expense involved was undoubtedly an element in the court's decision in Talley. It has been held that the relative financial resources of the party seeking information through the use of legal process and the non-party from whom information is sought is a key factor in determining which side should bear the expenses incurred in compiling the requested information. See United States v. Int'l Business Machines Corp., 62 F.R.D. 507, 510 (S.D.N.Y. 1974); 5A Moore, Federal Practice ¶45.05[2], page 45-50, 51, note 45 (2 ed. 1975).

under Eisen IV a class representative must pay the costs of reasonable notice even if they are burdensome, reasonable notice herein consists of mailing the notice to registered holders only, together with an instruction to nominees to notify beneficial holders. In consequence, considerations of the relative financial impact on the class representatives and on the individual nominees for activities over and above such reasonable notice is appropriate and fully consistent with Eisen IV.

(b) The District Court Below Erred in Holding That This Court's Decision in Sanders v. Levy Requires Class Representatives To Pay The Costs Involved

Judge Platt deemed the issue at bar controlled by this Court's decision in Sanders v. Levy, supra, stating:

> "With respect to the first of the two issues raised by the parties, there are two recent decisions in this Circuit, the first of which indicates and the second of which holds that the 'plaintiff, and not the brokerage firms, must bear the cost of notifying class members.' Sanders v. Levy, et al., ___ F.2d___ (2d Cir., Slip Op. 4577, June 30, 1976); Weiss v. Drew National Corporation, et al., ___ F.Supp.___, at p. (S.D.N.Y. 75 Civ. 4816, July 15, 1976).
>
> "In the Sanders case the plaintiffs were stockholders of a mutual fund who brought both class and derivative claims against the Fund's directors and investment advisor. For purposes of the derivative claims only, the Fund itself was joined as a nominal defendant but no class claims were

> asserted against it. The District Court imposed the costs of extracting the names and addresses of the class members from the Fund's magnetic tapes on the Fund. In reversing, the Court of Appeals held that it was 'totally improper to impose costs on the Fund' because the Fund was not a party to the class action claims (___F.2d___, at P. , Slip Op. at p. 4583).
>
> "If anything, the facts in the case at bar present an a fortiori situation to the facts in the Sanders case because here the brokerage firms whose customers comprise a part of the class are not as involved as the mutual fund might be said to have been in the Sanders case.
>
> "In addition, as indicated, the facts in the Weiss case appear to be on 'all fours' with those in the case at bar and Judge Stewart was of the opinion that the Court of Appeals decision in Sanders refusing to impose the costs on the mutal fund was determinative of the question presented here. We agree." (A225-A226)

Plaintiffs submit that the District Court below and Judge Stewart in Weiss v. Drew International Corp., et al., supra, (A172-A175),* were incorrect in interpreting Sanders v. Levy to require class representatives to pay the expenses of identifying beneficial owners of nominee name securities.

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* In light of the fact that Judge Stewart relied solely on Sanders v. Levy in holding that class representatives must pay the costs at issue (A173), it is clear that Judge Platt's decision was wholly determined by his interpretation of Sanders v. Levy.

In Sanders v. Levy, a divided panel of this Court required a class representative to reimburse Oppenheimer Fund, Inc. for its expenses incurred in compiling, from its computer tapes, a list of owners of Oppenheimer Fund securities as maintained by the Fund's transfer agent. Sanders v. Levy is inapplicable herein because it does not consider or deal with the issue of who should bear the burden of extra costs arising from registration of securities in street name or discuss the question whether, as held in cases such as In re Four Seasons Securities Laws Litigation, supra, and In re National Student Marketing Litigation, supra, class representatives fulfill their notice responsibilities under Eisen IV through a suitable notice to all record owners.

Thus, Sanders v. Levy requires only that the costs of culling the identities of registered owners from the defendant's transfer records be borne by the class representative. Moreover, the reasoning of the Sanders v. Levy opinion supports rejection of defendants' position in that Sanders v. Levy stressed that

> "We may not assume that non-class member shareholders would approve of the Fund underwriting these expenses for the benefit of other shareholders." 21 Fed.R.Serv.2d at 1216, ftn.3; Slip Opinion, p.4583, fn. 3 (A 157)

Similarly, the Court herein should not impose upon class members who did not purchase their securities in street name extra costs incurred solely because other class members and their brokers chose to obscure such class members' identities as beneficial owners.

Plaintiffs submit that the language in Sanders v. Levy which Judge Platt characterizes as a statement that "it was 'totally improper to impose costs on the Fund' because the Fund was not a party to the class action claims" (A 225), was intended by this Court to explain why the relationship between plaintiffs in Sanders v. Levy and the Fund did not justify an exception to the Eisen IV rule that plaintiffs must bear notification costs. See 21 Fed.R.Serv. 2d at 1216; Slip Opinion, p. 4583 (A 157). Consequently, Sanders v. Levy does not represent authority for the proposition that identification costs may not be assessed against a non-party in a situation in which Eisen IV does not require plaintiff to pay the costs at issue.

(c) Numerous Factors Demonstrate That it Would Be Unreasonable and Unfair to Impose Upon Class Representatives the Effort and Expense of Identifying and Providing Notice to Beneficial Owners of Unregistered Securities

(i) Notice To Record Owners Is Widely Recognized As Sufficient Notice With Respect To the Beneficial Owners

Under state law generally, notice to record owners of securities is regarded as sufficient to fulfill the responsibilities of the person who must provide notice to security owners. Thus, the Uniform Commercial Code, in force throughout the United States with the exception of Louisiana, permits an issuer or indenture trustee to "treat the registered owner as the person exclusively entitled to vote, to receive notifications and otherwise to exercise all the rights and powers of an owner." U.C.C. 8-207(1) (emphasis added).

Consistent with the above, record owners are generally recognized to be the owner of the securities involved for the purpose of asserting important corporate rights. Thus in Gruss v. Curtis Publishing Co., 534 F.2d 1396, 1402 (2d Cir. 1976), this Court recognized that

> "The most common rule is that objections giving rise to appraisal rights must be made by stockholders of record, just as voting rights can only be exercised by such holders." (footnote reference omitted; see cases cited in footnotes 10 and 11 on page 1402)

See also, Greenfield v. Villager Industries, 483 F.2d 824 (3rd Cir. 1973) (nominees had standing to challenge inadequate notice to class as legal owners of the shares involved); Drachman v. Harvey, 453 F.2d 722, 726 (2d Cir. 1971), in which the issue was whether a beneficial but unregistered owner had standing to bring a derivative action in light of a California statute restricting the right to bring a derivative action to registered owners.

(ii) Nominees Should Not Be Reimbursed For The Costs Of Carrying Out Their Fiduciary Obligation to Transmit Notices to Beneficial Owners of Stock in Nominee Name

The fiduciary duty of brokers (who are typically in possession of the relevant lists of unregistered class members) to the beneficial owners is well recognized:

> "A stock broker, acting as a broker for a customer, is, of course, in a fiduciary relation to the customer, since he is acting as agent, and he owes a duty of loyalty to the customer." 1 Scott, Trusts, page 134 (3rd ed. 1967)

The fiduciary duty of broker-dealers to carry out undertakings to their customers with the utmost good faith and care is widely recognized. E.g., Barnett v. United States, 319 F.2d 340, 344-45 (8th Cir. 1963); Opper v. Hancock Securities Corp., 250 F.Supp. 668, 673-75 (S.D.N.Y.), aff'd., 367 F.2d 157 (2d Cir. 1966); Selcow v. Floersheimer, 20 A.D.2d 889, 248 N.Y.S.2d 934 (1st Dept. 1964). Such a responsibility reflects the general duty of an agent to his principal

> "...to fully, fairly, and honestly disclose all material facts which come to his knowledge or attention, and which relate to the subject of the agency. McCormack v. Security Mutual Life Insurance Co., 220 N.Y. 447, 458, 116 N.E. 74; Casco National Bank of Portland v. Clark, 139 N.Y. 307, 313, 34 N.E. 908, 36 Am.St.Rep. 705; Henry v. Allen, 151 N.Y. 1, 9, 45 N.E. 355, 36 L.R.A. 658." Hurley v. John Hancock Mut. Life Ins. Co., 247 App. Div. 547, , 288 N.Y. Supp. 199, 203 (4th Dept. 1936).

Registration of securities in nominee name reflects the nominee's agreement with the beneficial owner that the nominee will serve as the beneficial owner's agent for the purpose of receiving important notices relating to the securities involved. See, e.g., Greenfield v. Villager Industries, Inc., supra, 483 F.2d at 829. Thus, in

its "Order and Instructions Concerning Notices to Brokers", the court in In re Clinton Oil Company Securities Litigation, supra, held that

> "[I]t is the initial duty of the Representatives to mail Notice and Proof of Claim form to the broker who is the record owner and holds legal title to securities, and that it is the duty of the broker to give notice to the beneficial owners. See Eisen v. Carlisle & Jacquelin, 417 U.S. 156, 40 L.Ed.2d 732 (1974); Greenfield v. Villager Industries, Inc., 483 F.2d 824 (3rd Cir. 1973)." Order, page 1. (emphasis added) See Exhibit C annexed to this brief.

The SEC has recognized that "depending on the facts and circumstances, the anti-fraud provisions of the federal securities laws may be applicable" to a broker's failure to transmit to its customer a notice from an issuer concerning redemption of securities. Karl E. Sommerlatte, [1971-72 Transfer Binder] CCH Fed.Sec.L.Rep., ¶78,557 (1971).*

Thus, defendants are requesting this Court to order the class to pay nominees for doing what the nominees

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* According to the SEC, nominee banks often refrain from seeking reimbursement for their expenses in distributing an issuer's material to beneficial owners because to do so might violate state trust laws which prohibit fiduciaries from profiting from administration of a trust. Street Name Study II, supra, page 21 and footnote 36.

are already obligated to do without compensation from plaintiffs -- i.e., advising their customers of a matter which significantly affects their interests and which falls directly within the scope of the agency which nominees have undertaken.

(iii) Nominees or their Customers, and Not the Class, Should Pay the Special Expenses Necessitated By Their Utilization of a System From Which The Nominees Derive Very Substantial Economic Benefits

As shown in detail above (see pages 10-11; 13-16), the system of nominee ownership has been developed and encouraged by the securities industry for its own purposes, and nominees derive extensive financial benefits from their customers' maintaining securities in nominee name. Nominees should not be permitted to foster a system for their own economic benefit which conceals the identity of the beneficial owner of securities and then receive reimbursement from class representatives to compensate them for costs necessitated by the very system they have created and encouraged. Thus, Judge Gurfein in Blank v. Talley Industries, Inc., supra, stated that a broker's expenses of identifying the beneficial owners of street name securities "are in the nature of

overhead expenses necessary for responding to legitimate court orders involving the customers of stock brokers" (54 F.R.D. at 627). See also Order and Instructions Concerning Notice to Brokers in In re Clinton Oil Company Securities Litigation, supra, p. 2 (Exhibit C annexed to this brief, p. 2) ("the cost or expense incurred by a broker in preparing a list of names, or in forwarding the Notices on behalf of his beneficial owners, is a cost or expense to be borne by the broker in conducting his business, and not by members of the plaintiff classes.")

As recognized in decisions such as In re Penn Central Securities Litigation, supra, (A 201-A 202); and Kushner v. Ampex Corp., supra, (Exhibit B annexed to this brief), the nominee and his customer enter into a private agreement for their own purposes when the customer chooses to place stock in nominee name. The special difficulty and expense of communications with the beneficial owner which results from such agreement should not be visited upon the class as a whole, but should be borne in the first instance by the nominees who can negotiate with their customers an

appropriate allocation of such expenses.*

(iv) Imposing the Costs at Issue On Class Representatives is Inconsistent With Public Policy Which Regards Securities Class Actions As a Key Device for Protection of Investors

As shown above (pages 16-18), the expenses involved herein represent a major economic burden which, if imposed on class representatives, would constitute a substantial impediment to the bringing of securities class actions generally. Consequently, the decision below threatens to have a severely detrimental impact on the ultilization of class actions, which actions are widely recognized by the courts to play a major role in securing compliance with the securities laws and protecting investors. E.g., Blackie v. Barrack, 524 F.2d 891, 903 (9th Cir. 1975); Kahan v. Rosenstiel, 424 F.2d 161, 169 (3d Cir.) cert. denied sub nom, Glen Alden Corp. v. Kahan, 398 U.S. 950 (1970); Esplin v. Hirschi, 402 F.2d 94, 101 (10th Cir. 1968), cert. denied, 394 U.S.

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* Thus the SEC found that banks typically do not request reimbursement from an issuer for forwarding proxy materials, but include the cost as a service charge to their customers. Special Study II, supra, p. 39.

928 (1969); Green v. Wolf Corp., 406 F.2d 291, 295, 301 (2d Cir. 1968), cert. denied, 395 U.S. 977 (1969); Eisen v. Carlisle & Jacquelin, 391 F.2d 555, 560 (2d Cir. 1968).

In Eisen v. Carlisle & Jacquelin, 391 F.2d 555, 560 (2d Cir. 1968) this Court declared:

> "Class actions serve an important function in our judicial system. By establishing a technique whereby the claims of many individuals can be resolved at the same time, the class suit both eliminates the possibility of repetitious litigation and provides small claimants with a method of obtaining redress for claims which would otherwise be too small to warrant individual litigation."

See also, Hohmann v. Packard Instrument Co., 399 F.2d 711, 715 (7th Cir. 1968).

In light of the numerous factors other than cost which show that requiring a class representative to identify unregistered owners for the purpose of sending them class notices would exceed the "reasonable effort" standard enunciated in Rule 23, this Court should not affirm an interpretation of Rule 23 which would severely undermine the effectiveness of class actions as an instrument of public policy. In State of West Virginia v. Chas. Pfizer & Co., Inc., 440 F.2d 1079, 1090 (2d Cir. cert. denied sub nom Cotler Drugs, Inc. v. Chas. Pfizer & Co., Inc., 404 U.S. 871

(1971), this Court emphasized that Rule 23(c)(2) does not require notice to all class members where such notice is not reasonably practicable, and cited with approval Judge Weinstein's statement in Dolgow v. Anderson, 43 F.R.D. 472, 497 (E.D.N.Y. 1968) that

> "In determining what constitutes 'the best notice practicable under the circumstances,' it is necessary to remember that the recent amendments were specifically designed to broaden the usefulness of the class action device.***By over emphasizing the notice requirement that purpose may be defeated."

Plaintiffs submit that an affirmance of the decision below would be in direct conflict with the purposes of Rule 23 as interpreted by this and other courts. No good reason appears for such a result, and the courts which have considered the question have rejected defendants' arguments with the exception of the two decisions which have misinterpreted this Court's decision in Sanders v. Levy. This Court should take the opportunity to clarify Sanders v. Levy in this regard and to reject the efforts of defendants and of nominees to severely inhibit class actions by the imposition of burdensome and unwarranted expenses on class representatives.

CONCLUSION

For the reasons stated above, the Court should reverse the Orders of October 27, 1976 and November 30, 1976

to the extent those Orders require plaintiffs to reimburse nominees for their expenses of identifying beneficial owners of nominee-name securities.

Dated: New York, New York
February 11, 1977

Respectfully submitted,

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Opinion, January 18, 1975, in
In Re Clinton Oil Company Securities Litigation,
MDL # 137 (D. Kan.), pp. 1, 30

EXHIBIT A

IN THE UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF KANSAS

IN RE CLINTON OIL COMPANY SECURITIES LITIGATION	M.D.L. No. 137
MARY d'O. SAURBREY, on behalf of herself and all others similarly situated, Plaintiff, vs. CLINTON OIL COMPANY, et al., Defendants.	Civil Action No. W-5430
SHIRLEY B. D'ALONZO, on behalf of herself and all others similarly situated, Plaintiff, vs. CLINTON OIL COMPANY, et al., Defendants.	Civil Action No. W-5083

MEMORANDUM AND ORDER

These cases allege violations of the Securities Act of 1933, the Securities Exchange Act of 1934, and the regulations of the Securities Exchange Commission by various defendants including Clinton Oil Company, its officers and directors. Certain defendants have filed motions to decertify the classes established by Court order and to quash the notice of a proposed settlement between Clinton Oil Company and members of such classes. Having considered the evidence and records before the Court, we make the following findings and order.

I. SAURBREY'S STANDING AND THE STATUTE OF LIMITATIONS

Mrs. Saurbrey filed an eleven-count amended complaint wherein she alleged ten counts of statutory and regulatory violations and one count of breach of fiduciary duties. The defendants have moved to decertify the class for the reasons, *inter alia*, that she lacks standing and/or the action is barred by the statute of limitations.

Furthermore, we are of the opinion that under Rule 23(c)(2) and *Eisen v. Carlisle & Jacqualin*, _____U.S._____, 42 U.S.L.W. 4804 (1974), those members of the classes "who can be identified through reasonable effort" and, thus, who should receive actual notice, are those members whose securities were registered on the books of Clinton Oil Company during the relevant times alleged in the complaints. A portion of the securities involved, we are infomred, were registered in "street name," that is in the name of a broker/dealer for the benefit of the owner. Although it may be possible to trace the ownership of the stock through the ledgers of the various broker/dealers and thereby give notice to the beneficial owner, such an effort would be unreasonable and not practicable. We are satisfied that the "process," as stated in *Eisen*, that is due to the beneficial owners of securities held in "street name" is actual notice to the registered owner and constructive notice to the beneficial owners by publication.

For the reasons hereinbefore stated,

IT IS BY THE COURT ORDERED:

1. That Counts Three, Four, Five, Seven, Eight, Nine, and Ten of the Saurbrey complaint (Case No. W-5430) be, and are hereby dismissed.

2. That Counts One and Two of the Saurbrey complaint, insofar as they pertain to the conduct of the defendants occurring after July 3, 1969, be, and are hereby, dismissed.

3. That Count Eleven of the Saurbrey complaint be, and is hereby, excluded from the class certification.

4. That the Saurbrey class with respect to Counts One, Two and Six is hereby redefined and subdivided as follows:

a. With respect to Counts One and Two, the class shall include all persons, excluding the individual defendants named herein, who purchased (or otherwise acquired) or sold (or otherwise disposed of) Clinton Oil Company common stock from January 26, 1966, to July 3, 1969.

Transcript of Hearing in
Kushner v. Ampex Corporation,
C 72-360 SW (N.D. Cal), p. 16

EXHIBIT B

is consummated.

MR. BERGER: I advised my office to tell the bank that the money should be put in Government securities. So that's where we are. The case is final and I think that the Hutton question is one which really is irrelevant at this time.

THE COURT: Thank you, Mr. Lambros and Mr. Albrecht.

Well, it is a very interesting question, but I would say that the last group to have paid the cost of extra efforts to search out those who own the stock that are held in street name would be the class. The primary person responsible should be the shareholder who is going to benefit by the judgment. And if E. F. Hutton and Company cannot by virtue of its authority or its power, either one, get reimbursement from their clients or former clients, I think then the burden is with them.

The motion is denied.

MR. BENVENUTTI: Very well, Your Honor.

MR. BERGER: Your Honor, may I just have another moment or two to take care of an administrative matter. I would like to submit this to Your Honor, if I may.

Your Honor, we now have well over 21,000 claims to process. We feel that, although Your Honor's order requires that every claim must be accompanied by a proof of purchase and it has to be notarized, that if a claim, as is the case

Order and Instructions Concerning Notice to Brokers, April 5, 1976 in In Re Clinton Oil Company Securities Litigation, MDL # 137 (D. Kan)

EXHIBIT C

IN THE UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF KANSAS

IN RE

CLINTON OIL COMPANY
SECURITIES LITIGATION

M.D.L. No. 137

ORDER AND INSTRUCTIONS CONCERNING
NOTICE TO BROKERS

Alexander B. Mitchell and Irving Morris, class action representatives appointed by the Court for the purpose of processing notices and proofs of claims in this action, have petitioned the Court for instructions concerning problems which have arisen in connection with Notices sent to broker-dealers holding Clinton Oil Company and Real Company securities in "street name." It appears that some brokers have refused to cooperate with Representatives and have made demand upon them for fees and expenses in connection with securities which they hold in trust for the benefit of undisclosed owners.

After review of the Report and Motion filed by the Representatives (Dkt. 908), the Court determines that it is the initial duty of the Representatives to mail Notice and Proof of Claim form to the broker who is the record owner and holds legal title to securities, and that it is the duty of the broker to give notice to the beneficial owners. See *Eisen v. Carlisle*

& Jacquelin, 417 U.S. 156, 40 L.Ed.2d 732 (1974); *Greenfield v. Villager Industries, Inc.*, 483 F.2d 824 (3d Cir. 1973).

When the Broker submits a list of names and addresses to the Representatives, disclosing the identity of the beneficial owners of the securities, it then becomes the duty of the Representatives to forward the Notice and Proof of Claim form to each such beneficial owner.

In the event a broker requests additional supplies of notices and proofs of claim forms for forwarding to the beneficial owners of street-name securities, the Representatives may then provide such forms to the broker. *Mullane v. Central Hanover Bank & Trust Co.*, 339 U.S. 306, 94 L.Ed. 865 (1950). However, the cost or expense incurred by a broker in preparing a list of names, or in forwarding the Notices on behalf of his beneficial owners, is a cost or expense to be borne by the broker in conducting his business, and not by the members of the plaintiff classes. See *Blank v. Talley-Industries, Inc.* (S.D.N.Y. 1972) 54 F.R.D. 627. Accordingly, the Court determines that the following procedures shall be in effect with respect to notices directed to brokers holding securities in street names for the benefit of undisclosed owners.

IT IS ORDERED that when a broker holds or held Clinton Oil Company or Real securities in street name, and requests additional sets of the Notice and Proof of claim form, the Representatives

shall provide the broker with a sufficient number of these forms, together with a sufficient number of envelopes, so that the broker may forward them to the beneficial owners for whom the broker holds, or held the securities in street name.

IT IS FURTHER ORDERED that when a broker submits a list of names and addresses of beneficial owners, the Representatives shall cause a Notice and Proof of Claim form to be mailed, postage prepaid, to each such beneficial owner.

IT IS FURTHER ORDERED that when a broker refuses to search its records for names and addresses of beneficial owners without first receiving an hourly and/or fixed fee, the Representatives shall refuse any such demand and shall notify the broker in writing that the NOtice recieved by the broker is and shall be considered by the Representatives as Notice to all of the broker's customers, both past and present, who have been or are beneficial owners of Clinton Oil Company or Real securities and who may be members of the classes entitled to participate in the distribution of the Settlement Fund.

IT IS FURTHER ORDERED that when a broker, after preparing a list of names and addresses of beneficial owners or after forwarding the Notice and Proof of Claim form to each such beneficial owners makes demand for expenses and/or fees, the Representative shall refuse any such demand and shall so notify the broker in writing.

At Wichita, Kansas this 5th day of April, 1976.

Chief Judge

STATE OF NEW YORK)
) SS.:
COUNTY OF NEW YORK)

YVETTE KARPO being duly sworn, deposes and says that she is in the employ of Milberg & Weiss, attorneys for the within named Plaintiff-Appellant, Robert Gold herein, and is over the age of 21 years. That on the 11th day of February, 1977, she served two (2) copies of the within Brief For Plaintiffs-Appellants upon the attorneys for the respective parties named on Attachment "A" by depositing a true copy of the same to each of them, securely enclosed in postpaid wrappers in a post office box regularly maintained by the United States Government at One Pennsylvania Plaza, New York, New York, directed to each of them at their respective addresses set forth below, those being the addresses within the State designated by them for that purpose on the preceding papers in this action, or the places where they then kept their respective offices between which places there then was and now is a regular communication by mail:

SEE ATTACHMENT "A"

Yvette Karpo
YVETTE KARPO

Sworn to before me this
11th day of February, 1977

Judith Goodhart
Notary Public

JUDITH GOODHART
Notary Public, State of New York
No. 41-4630261
Qualified in Queens County
Commission Expires March 30, 1978

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ATTACHMENT "A"

Time Received

FROM 2 GAITHER

Howard Crosse

February 11, 1977

4:50 P.M.

R.W.